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Drink Deep or Taste Not

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"A little learning is a dangerous thing,
Drink deep, or taste not the Pierian spring."

Alexander Pope, "Essay on Criticism" (1711)

Augustan poetry may not be to your taste, but Pope's rhyming couplet contains a truth that is often forgotten by investors. It is important to know and understand what you are invested in and equally important to recognise and understand the limits of what you do know.

So much of stockmarket and investment commentary is hearsay, speculation, and snake oil that it can be all too easy to get caught up in the speculative frenzy of the day and to lose sight of the fundamentals: sales growth, cashflow, balance sheet, profits, and dividends. Even one of the most brilliant minds in our history, and Pope's contemporary, Sir Isaac Newton, got caught up in the famous bubble of his time, the South Sea Bubble, and lost his fortune, equivalent to £3 million today.

None of us is expert across all aspects of human endeavour, even the man who invented calculus.

Behavioural economists point to what they call "loss aversion," as a powerful driver of investor behaviour. In most circumstances we tend to experience the pain of loss more deeply than the anticipation and pleasure of gain.

On the other hand, occasionally events accumulate around us and that loss aversion flips into what is known as FOMO – "fear of missing out" where, perhaps, friends or colleagues seem to make lots of money in unfamiliar ways, and we want to participate. When that happens, as it clearly did to Sir Isaac (he cashed in his South Sea shares at a large profit but then envious of further gains he bought back in at the peak of the bubble), investors seem to lose all sense of loss aversion; it is as if a switch has been flipped.

Having been practitioners in the investment industry since the mid-1980s, we have seen our fair share of investor fads, fashions, and frenzies. It is fascinating that at certain times investors' willingness to invest in things (anything) is exactly inverse to what they know about what they are investing in.

In the 1980s everybody wanted the Asian Tigers, even though it was vague what and where they were to most people. In the pre-internet age, which somewhat unbelievably is as recent as the 1990s, merely appending "dot.com" to the name of a company was enough to send the share price flying. More recently, Elon Musk achieved a similar feat. When he suggested on a tweet that people should use "Spring" to communicate rather than WhatsApp, a company called Spring Inc. entirely unrelated to either Musk or the communications industry, rose 1000% in one day before falling back.

The reason why Holland has a vibrant fresh flower industry today is the Tulip mania of the 17^{th} century when single tulip bulbs were exchanging hands for the price of a house. An unfortunate servant ate one with his lunch mistaking it for an onion with consequences too painful to relate.

Since the turn of the century investors have seen gold, as it were, in esoteric issues such as CDOs (collateralised debt obligations) and CLO's (collateralised loan obligations) sometimes "squared" and occasionally "cubed."

Today we have the rise of Bitcoin, Tether, Ethereum and, this may be a surprise, some 7,997 other varieties of crypto-currency, and growing. This is interesting because one of the fundamental attractions of Bitcoin was that the issuance was limited to 21 million (digital) coins. It turns out that this fundamental grounding of the new digital revolution is baseless: there is no limit to the issuance of crypto. If the supply of coin is infinite, what value can one put upon it?

Finally, we have the rise of the NFT – "non fungible token" – which, for the moment is probably best represented by the "Bored Ape Yacht Club." These are cartoon pictures of, well, bored looking apes that are selling over the internet for $295,000 apiece. You don't buy the picture, you buy the code, over the blockchain, that links to the picture.

Looked at from an art history perspective where authenticity is found in uniqueness – there is only one Mona Lisa which is irreducible despite the many reproductions of it – the NFT world turns that relationship upside down. That there are many reproductions of the bored ape is immaterial; there is only one code.

Who knows, and we don't, despite having all the hallmarks of previous investor bubbles, NFTs and Crypto might be the future but like Warren Buffett's attitude to space flight, "we can applaud the endeavour, but we don't need to go along for the ride." We are occasionally criticised for being a bit conservative. But investment management is littered with examples of what goes wrong when managers go off-piste.

At the end of the story alluded to by Alexander Pope, the Pierides are transformed into Magpies, birds famous for collecting things that glint but which have no knowledge of value. This is a lesson that we hope many of our clients will understand, and will trust our experience to help navigate them through over the coming years.